



STATE OF INDIANA

AN EQUAL OPPORTUNITY EMPLOYER

B40468

STATE BOARD OF ACCOUNTS
302 WEST WASHINGTON STREET
ROOM E418
INDIANAPOLIS, INDIANA 46204-2765

Telephone: (317) 232-2513
Fax: (317) 232-4711
Web Site: www.in.gov/sboa

June 1, 2012

Board of Directors
Johnson Memorial Hospital
1125 W. Jefferson Street
P.O. Box 549
Franklin, IN 46131

We have reviewed the audit report prepared by Blue & Co., LLC, Independent Public Accountants, for the period January 1, 2011 to December 31, 2011. In our opinion, the audit report was prepared in accordance with the guidelines established by the State Board of Accounts. Per the Independent Public Accountants' opinion, the financial statements included in the report present fairly the financial condition of the Johnson Memorial Hospital, as of December 31, 2011 and the results of its operations for the period then ended, on the basis of accounting described in the report.

The Independent Public Accountants' report is filed with this letter in our office as a matter of public record.

STATE BOARD OF ACCOUNTS



CONSOLIDATED FINANCIAL STATEMENTS
AND
REQUIRED SUPPLEMENTARY INFORMATION
DECEMBER 31, 2011 AND 2010

CPAs / ADVISORS



JOHNSON MEMORIAL HOSPITAL

TABLE OF CONTENTS DECEMBER 31, 2011 AND 2010

	Page
Report of Independent Auditors	1
Required Supplementary Information	
Management's Discussion and Analysis (Unaudited)	i
Consolidated Financial Statements	
Consolidated Balance Sheets	3
Consolidated Statements of Revenues, Expenses and Changes in Net Assets	5
Consolidated Statements of Cash Flows	6
Notes to Consolidated Financial Statements	8



Blue & Co., LLC / One American Square, Suite 2200 / Box 82062 / Indianapolis, IN 46282
main 317.633.4705 fax 317.633.4889 email blue@blueandco.com

REPORT OF INDEPENDENT AUDITORS

Board of Trustees
Johnson Memorial Hospital
Franklin, Indiana

We have audited the accompanying consolidated balance sheets of Johnson Memorial Hospital (the Hospital) as of December 31, 2011 and 2010 and the related consolidated statements of revenues, expenses and changes in net assets and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America and Guidelines for Audits of County and City Hospitals by Independent Certified Public Accountants, issued by the Indiana State Board of Accounts. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above, present fairly, in all material respects, the consolidated financial position of the Hospital as of December 31, 2011 and 2010, and its results of operations, changes in net assets and cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis be presented to supplement the basic consolidated financial statements. Such information, although not a part of the basic consolidated financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic consolidated financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States

Board of Trustees
Johnson Memorial Hospital
Franklin, Indiana

of America which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic consolidated financial statements, and other knowledge we obtained during our audit of the basic consolidated financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Blue & Co., LLC

March 27, 2012

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

This section of Johnson Memorial Hospital's (the Hospital) annual consolidated financial statements presents background information and management's discussion and analysis of the Hospital's financial performance during the year ended December 31, 2011. This MD&A includes a discussion and analysis of the activities and results of the Johnson County Health Foundation (blended component unit).

This MD&A should be read together with the consolidated financial statements included in this report.

FINANCIAL HIGHLIGHTS

- The Hospital's net assets increased by \$1.1 million, and include operating income of \$1.7 million in 2011.
- The Hospital's total net operating revenue remained relatively flat at \$77.0 million compared against \$77.1 million in 2010 while expenses decreased by 1.2% to \$75.3 million. The resulting income from operations of \$1.7 million represents an increase of nearly double 2010 operations.
- The Hospital's total non-operating revenue decreased from a gain of \$337,000 in 2010 to a loss of \$575,000 in 2011 due mainly to decreased market performance on Plant Fund investments; decreased interest income on cash investments; as well as due to a transfer of Gift Fund monies to the Foundation.

FINANCIAL STATEMENTS

The Hospital's consolidated financial statements consist of three statements - a Balance Sheet; a Statement of Revenues, Expenses and Changes in Net Assets; and a Statement of Cash Flows. The Balance Sheet includes all of the Hospital's assets and liabilities, including assets held by the Hospital but designated for specific purposes by contributors, grantors, or enabling legislation. The Balance Sheet provides a basis for computing rate of return, evaluating the capital structure of the Hospital, and assessing the liquidity and financial flexibility of the Hospital. The Statement of Revenues, Expenses and Changes in Net Assets includes all revenues and expenses of the Hospital. This statement measures the financial results of the Hospital's operations and presents revenue earned and expenses incurred. The Statement of Cash Flows provides information about the Hospital's cash flows from operating activities, capital and related financing activities, and investing activities, and provides information on the sources and uses of cash during the year.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

FINANCIAL ANALYSIS

One of the most important questions asked about the Hospital's finances is, "Is the Hospital as a whole better or worse off as a result of the year's activities?" The balance sheet and the statement of revenues and expenses report information about the Hospital's resources and its activities in a way that helps answer this question. These statements include all designated and unrestricted assets and all liabilities using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the Hospital's net assets and changes in them. Think of the Hospital's net assets — the difference between assets and liabilities — as one way to measure the Hospital's financial health, or financial position. Over time, increases or decreases in the Hospital's net assets are one indicator of whether its financial health is improving or deteriorating. Consider other nonfinancial factors, however, such as changes in the Hospital's patient base and measures of the quality of service it provides to the community, as well as local economic factors to assess the overall health of the Hospital.

A summary of the Hospital's Balance Sheets as of December 31, 2011 and 2010 is presented below (in thousands):

	2011	2010	2011 - 2010 Change	2009
Cash and investments	\$ 36,217	\$ 36,694	\$ (477)	\$ 36,958
Capital assets	43,318	39,709	3,609	40,079
Other assets	15,926	17,611	(1,685)	17,130
Total assets	<u>\$ 95,461</u>	<u>\$ 94,014</u>	<u>\$ 1,447</u>	<u>\$ 94,167</u>
Current and other liabilities	\$ 8,070	\$ 7,331	\$ 739	\$ 7,974
Long term debt	1,973	2,386	(413)	3,083
Total liabilities	10,043	9,717	326	11,057
Net assets				
Invested in capital assets, net of related debt	40,567	36,626	3,941	35,619
Designated	23,070	26,367	(3,297)	25,887
Unrestricted	21,781	21,304	477	21,604
Total net assets	<u>85,418</u>	<u>84,297</u>	<u>1,121</u>	<u>83,110</u>
Total liabilities and net assets	<u>\$ 95,461</u>	<u>\$ 94,014</u>	<u>\$ 1,447</u>	<u>\$ 94,167</u>

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

As displayed above, total net assets increased to \$85.4 million in 2011, up from \$84.3 million in 2010. The change in net assets resulted primarily from operating gains and minor investment income as well. Investment income in 2011 was considerably lower than in 2010 due to a relatively weak year in the Hospital's fund performance and to the Hospital's conservative approach in its investment strategy during 2011.

A summary of the Hospital's Statement of Revenues, Expenses and Changes in Net Assets for 2011 and 2010 is presented below (in thousands):

	2011	2010	2011 - 2010 Change	2009
Revenue				
Net patient service revenue	\$ 67,211	\$ 67,433	\$ (222)	\$ 67,089
Other	9,788	9,627	161	9,251
Total revenue	76,999	77,060	(61)	76,340
Expenses				
Salary and benefits	42,162	41,324	838	40,493
Supplies and other	28,951	30,645	(1,694)	30,089
Depreciation and amortization	4,189	4,241	(52)	4,536
Total operating expenses	75,302	76,210	(908)	75,118
Operating income	1,697	850	847	1,213
Non-operating revenue (expense)	(575)	337	(912)	1,005
Change in net assets	\$ 1,122	\$ 1,187	\$ (65)	\$ 2,218

STATEMENTS OF CASH FLOWS

The final required statement is the statement of cash flows. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and financing activities. It provides answers to such questions as "Where did cash come from?" "What was cash used for?" and "What was the change in cash balance during the reporting period?" A summary of cash flows for 2011 and 2010 follows (in thousands):

	2011	2010	2011-2010 Change	2009
Cash flow from activities				
Operating	\$ 8,043	\$ 4,519	\$ 3,524	\$ 3,083
Capital and related financing	(8,628)	(5,739)	(2,889)	(5,288)
Investing	9,457	11,103	(1,646)	6,731
Change in cash equivalents	\$ 8,872	\$ 9,883	\$ (1,011)	\$ 4,526

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

Total cash and cash equivalents increased by \$8.9 million in 2011. Operating activities generated cash and cash equivalents of \$8.0 million during 2011. Capital and related financing impacted cash and cash equivalents by \$8.6 million during 2011 mainly as the result of property and equipment additions consolidated with principal payments on long-term debt. The Hospital's capital related activities include the fact that cash was not borrowed to finance the Surgery expansion project that was underway during 2011. Investing activities increased cash and cash equivalents by \$9.5 million mainly as a result of proceeds from investments to purchase cash equivalents.

SOURCES OF REVENUE

During 2011, the Hospital derived substantially all of its revenue from patient services and other related activities. Revenue includes, among other items, revenue from the Medicare and Medicaid programs, patients, insurance carriers, preferred provider organizations, and managed care programs.

The table below presents the percentages of gross revenue for patient services, by payor, for 2011 and 2010.

<u>Payor Mix</u>	<u>2011</u>	<u>2010</u>
Medicare	45%	43%
Medicaid	10%	10%
Blue Cross/Anthem	17%	17%
Commercial insurance	19%	21%
Self-pay	8%	8%
Other	1%	1%
Total	<u>100%</u>	<u>100%</u>

The Hospital entered into agreements with third party payers, including government programs and managed care health plans, under which payments for healthcare services provided to patients are based upon predetermined rates or discounts from gross charges. Provisions have been made in the financial statements for contractual adjustments, which represent the difference between the standard charges for services and the actual or estimated payment.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

OPERATING AND FINANCIAL PERFORMANCE

Overall, the Hospital's financial performance in 2011 was stronger than 2010. This section discusses highlights of 2011 operations and changes in activities.

(a) Revenue

- Net patient revenues decreased by .3% in 2011 compared to 2010. Hospital outpatient revenues were 5.9% greater than 2010 while inpatient revenues were nearly 3.1% higher. When considering the 6% price increase, inpatient revenues remained compressed due to several factors: (a) the continued suppressed economy; (b) the continuing shift in the delivery of inpatient medical care to the observation/outpatient/physician practice setting coupled with a lower number of patient days; and, (c) the impact of losing a key surgical specialist in mid-2011. Outpatient revenues, factoring in the price increase, were essentially flat from the previous year. Deductions from revenue for contractual allowances and bad debts increased 9.0% in 2011 offsetting the inpatient and outpatient increases.
- Acute inpatient volume, as measured in terms of admissions, increased to 2,474 in 2011 from 2,438 in 2010, or (1.5%).
- Acute rehabilitation volume, as measured in terms of admissions, increased to 198 in 2011 from 184 in 2010, or 7.6%.
- Outpatient volumes were flat. Gross outpatient charges increased by 5.9% over 2010, which is essentially related to the 6% rate increase.
- Excluded from net patient revenue are charges for patient services waived under the Hospital's charity policy. Charity care represents unreimbursed charges incurred by the Hospital in providing uncompensated care to indigent patients. Based on established rates, gross charges of \$6.6 million were waived in 2011 compared to \$6.4 million in 2010. These amounts represent a relatively consistent write-off percent of gross patient charges between the two years with 2011 slightly more favorable than 2010 (i.e., 3.7% in 2011 vs. 3.8% in 2010).

(b) Expenses

- Total operating expenses decreased \$908,000 or 1.2% in 2011 primarily due to decreased supply costs. Supply costs were lower related to the discontinuation of certain high-cost procedures performed in the operating suite.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

- Employee labor and benefit expenses increased \$838,000 or 2% over 2010. This is mostly attributable to a modest cost-of-living increase granted to staff in 2011.
- Provision for bad debt decreased \$175,000 or 3.2% over 2010. This amount represented 3.0% of gross patient charges compared to 3.3% the previous year. The combined charity care/bad debt write-offs as a percent of Hospital gross patient revenues decreased from 7.1% in 2010 to 6.7% in 2011.
- Depreciation and amortization expenses remained relatively constant over 2010.

CAPITAL ASSETS

During 2011, the Hospital's capital assets increased by \$3.6 million due to capital additions and construction in progress outpacing depreciation. This is mostly driven by the new Surgery Center expansion project. The below table summarizes the broad categories (in thousands):

	2011	2010	2011-2010 Change	2009
Land and improvements	\$ 4,630	\$ 4,604	\$ 26	\$ 4,532
Buildings and improvements	55,311	56,480	(1,169)	56,249
Equipment	41,788	40,370	1,418	38,238
Construction in progress	6,874	1,750	5,124	1,681
Total capital assets	108,603	103,204	5,399	100,700
Less accumulated depreciation	65,284	63,494	1,790	60,621
Capital assets - net	\$ 43,319	\$ 39,710	\$ 3,609	\$ 40,079

LONG TERM DEBT

As of December 31, 2011, the Hospital had \$2.75 million in short term and long-term notes and bonds, a decrease of \$332,000 from the \$3.08 million as of December 31, 2010. More detailed information about the Hospital's debt position is presented in the Notes to the Consolidated Financial Statements.

JOHNSON MEMORIAL HOSPITAL

MANAGEMENT'S DISCUSSION & ANALYSIS (UNAUDITED) DECEMBER 31, 2011 AND 2010

ECONOMIC FACTORS AND 2012 BUDGET

The Hospital's Board and management considered many factors when establishing the 2012 Budget. Factors considered included, among other things, the following items:

- Population growth trends of Johnson County, Indiana and the Hospital's current market share of county residents
- Expansion of the surgical suite area to include advances in medical equipment and technology. Also considered was the need to replace obsolete equipment and improve the IT infrastructure and electronic health record capability in order to meet Federal criteria under the Medicare and Medicaid Healthcare IT incentive programs
- Decreasing reimbursement from governmental and commercial insurance payers as well as the continued unfavorable governmental payer mix the Hospital is experiencing
- Continued high number of uninsured, underinsured and/or indigent patients
- Increasing costs of physician practices and related technology, medical supplies, and pharmaceuticals
- Increasing emphasis on clinical, administrative and financial collaborations with independent entities for services the Hospital is not capable of implementing on its own when addressing the challenges of the pending National Healthcare Reform Act
- Increasing awareness and expectations from the public on the quality of services
- Continued increased competition from niche and physician providers as well as the continued expansion of the major Indianapolis providers of healthcare into the Johnson County market (i.e., St. Francis, Community Health Network and IU Health)

CONTACTING THE HOSPITAL'S FINANCIAL MANAGEMENT

This report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Hospital's finances and to show the Hospital's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Hospital's Chief Financial Officer, Elizabeth A. Hedden, at Johnson Memorial Hospital, P.O. Box 549, Franklin, Indiana 46131.

JOHNSON MEMORIAL HOSPITAL

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2011 AND 2010

ASSETS

	2011	2010
Current assets		
Cash and cash equivalents	\$ 12,144,615	\$ 10,326,119
Investments	1,000,000	-0-
Assets whose use is limited, current portion	778,624	697,649
Patient accounts receivable, net of allowance for uncollectible accounts of \$4,197,000 in 2011 and \$4,259,000 in 2010	11,235,581	13,173,900
Other accounts receivable	1,286,035	1,338,070
Inventory and other current assets	3,125,603	2,814,571
Estimated third-party settlements	178,912	-0-
Current portion of notes receivable	49,490	80,556
Total current assets	29,798,860	28,430,865
Assets whose use is limited		
Internally designated	21,529,665	24,832,597
Held by Foundation	1,542,440	1,534,855
Total assets whose use is limited	23,072,105	26,367,452
Less current portion	778,624	697,649
Noncurrent assets whose use is limited	22,293,481	25,669,803
Capital assets		
Land	3,141,963	3,141,963
Depreciable capital assets, net	40,176,547	36,566,887
Total capital assets, net	43,318,510	39,708,850
Investment in affiliates	50,105	203,570
Total assets	\$ 95,460,956	\$ 94,013,088

See accompanying notes to consolidated financial statements.

JOHNSON MEMORIAL HOSPITAL

CONSOLIDATED BALANCE SHEETS DECEMBER 31, 2011 AND 2010

LIABILITIES AND NET ASSETS

	2011	2010
Current liabilities		
Accounts payable and accrued expenses	\$ 2,226,998	\$ 2,013,392
Accrued wages and related liabilities	5,041,387	4,511,960
Estimated third-party settlements	-0-	85,365
Current portion of long term debt	778,624	697,649
Other current liabilities	22,493	22,493
Total current liabilities	8,069,502	7,330,859
Long term debt, net of current portion		
Capital lease obligations	245,199	-0-
Loans payable	1,727,630	2,385,554
Total long term debt	1,972,829	2,385,554
Total liabilities	10,042,331	9,716,413
Net assets		
Invested in capital assets, net of related debt	40,567,057	36,625,647
Designated		
Expendable - funded depreciation	18,210,393	13,735,138
Expendable - capital improvements	1,868,509	5,784,553
Expendable - other board designated	1,450,763	5,312,906
Held by Foundation	1,540,755	1,534,855
Total designated net assets	23,070,420	26,367,452
Unrestricted	21,781,148	21,303,576
Total net assets	85,418,625	84,296,675
Total liabilities and net assets	\$ 95,460,956	\$ 94,013,088

See accompanying notes to consolidated financial statements.

JOHNSON MEMORIAL HOSPITAL

CONSOLIDATED STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
Revenues		
Net patient service revenue	\$ 67,210,870	\$ 67,433,021
Other revenue	9,788,174	9,626,913
Total revenues	76,999,044	77,059,934
Expenses		
Salaries and wages	34,001,263	33,075,766
Employee benefits	8,161,123	8,248,130
Medical professional fees	976,278	938,832
Other professional fees	5,124,638	5,647,670
Medical supplies and drugs	11,587,866	12,043,530
Other supplies	841,123	866,839
Depreciation and amortization	4,188,850	4,241,118
Insurance	989,974	1,121,879
Other expenses	9,431,373	10,025,922
Total expenses	75,302,488	76,209,686
Operating income	1,696,556	850,248
Nonoperating revenues (expenses)		
Investment income	63,137	698,637
Interest expense	(134,279)	(167,751)
Rental revenue (expense), net	(394,949)	(371,912)
Foundation - primarily investment income	5,900	122,725
Other nonoperating income (expense)	(114,415)	54,979
Nonoperating revenues (expenses), net	(574,606)	336,678
Change in net assets	1,121,950	1,186,926
Net assets		
Beginning of year	84,296,675	83,109,749
End of year	<u>\$ 85,418,625</u>	<u>\$ 84,296,675</u>

See accompanying notes to consolidated financial statements.

JOHNSON MEMORIAL HOSPITAL

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
Operating activities		
Cash received from patient services	\$ 68,884,912	\$ 66,733,419
Cash paid for salaries, wages and benefits	(41,632,959)	(41,631,242)
Cash paid to vendors and suppliers	(29,007,829)	(31,130,726)
Other receipts, net	9,799,360	10,547,135
Net cash flows from operating activities	8,043,484	4,518,586
Capital and related financing activities		
Receipts on notes receivable, net	31,066	54,457
Payments on long term debt, net	(728,123)	(1,377,184)
Interest on long term debt	(134,279)	(167,751)
Gain on disposal of equipment	(11,186)	-0-
Purchase of capital assets	(7,821,856)	(4,280,457)
Proceeds from disposal of equipment	35,896	32,283
Net cash flows from capital and related financing activities	(8,628,482)	(5,738,652)
Investing activities		
Investment income	63,137	698,637
Rental revenue (expenses), net	(394,949)	(371,912)
Foundation investment income	5,900	122,725
Other nonoperating revenue (expense)	(114,415)	54,979
Proceeds from sale of investment in affiliates	149,000	-0-
Proceeds from sale of investments	15,771,965	16,723,781
Purchase of investments	(6,024,133)	(6,125,583)
Net cash flows from investing activities	9,456,505	11,102,627
Net change in cash and cash equivalents	8,871,507	9,882,561
Cash and cash equivalents		
Beginning of year	20,845,080	10,962,519
End of year	<u>\$ 29,716,587</u>	<u>\$ 20,845,080</u>
Reconciliation of cash and cash equivalents		
to the balance sheets		
Cash and cash equivalents		
In current assets	\$ 12,144,615	\$ 10,326,119
In assets whose use is limited	17,512,674	10,380,576
In held by Foundation	59,298	138,385
Total cash and cash equivalents	<u>\$ 29,716,587</u>	<u>\$ 20,845,080</u>

See accompanying notes to consolidated financial statements.

JOHNSON MEMORIAL HOSPITAL

CONSOLIDATED STATEMENTS OF CASH FLOWS YEARS ENDED DECEMBER 31, 2011 AND 2010

	2011	2010
Reconciliation of operating income to net cash from operating activities		
Operating income	\$ 1,696,556	\$ 850,248
Adjustments to reconcile operating income to net cash flows from operating activities		
Depreciation and amortization	4,188,850	4,241,118
Bad debts	5,375,360	5,550,245
Changes in operating assets and liabilities		
Patient accounts receivable	(3,437,041)	(6,246,846)
Other accounts receivable	52,035	275,580
Inventory and other current assets	(311,032)	(188,411)
Accounts payable and accrued expenses	213,606	394,695
Accrued wages and related liabilities	529,427	(307,346)
Estimated third-party settlements	(264,277)	(49,435)
Other current liabilities	-0-	(1,262)
Net cash from operating activities	<u>\$ 8,043,484</u>	<u>\$ 4,518,586</u>
Supplemental disclosure of cash flows		
Cash paid for interest	\$ 134,279	\$ 167,751
Property acquired through capital lease	\$ 396,372	\$ -0-

See accompanying notes to consolidated financial statements.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

Johnson Memorial Hospital (the Hospital) is an acute-care hospital located in Franklin, Indiana, organized for the purpose of providing healthcare services to the residents of Johnson County and the surrounding communities. The Hospital is a county-owned facility and operates under the Indiana County Hospital Law, Indiana Code (IC) 16-22. The Hospital provides short-term inpatient and outpatient health care, skilled nursing and intermediate care and emergency care.

The Board of County Commissioners of Johnson County appoints the Governing Board of the Hospital. The Hospital is considered a component unit of Johnson County.

The consolidated financial statements of Hospital are intended to present the financial position and the changes in financial position and cash flows of only that portion of the business-type activities of Johnson County that is attributable to the transactions of the Hospital and its Foundation. They do not purport to, and do not, present fairly the financial position of Johnson County as of December 31, 2011 and 2010, the changes in its financial position or its cash flows for the years then ended.

Accounting principles generally accepted in the United States require that these consolidated financial statements present the Hospital and its significant component units, collectively referred to as the "primary government." The blended component unit discussed below is included in the Hospital's reporting entity because of the significance of their operational or financial relationships with the Hospital. Blended component units, although legally separate entities are in substance part of the primary government's operations and exist solely to provide services for the primary government; data from these units is consolidated with data of the primary government.

Blended Component Unit

The accompanying consolidated financial statements include the accounts of Johnson County Health Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of the Hospital. All intercompany accounts and transactions between the primary government and its blended component unit have been eliminated in the consolidation.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The separate financial statements of the Foundation may be obtained through contacting their office as follows:

Johnson County Health Foundation, Inc.
1101 W. Jefferson St., Ste. V
Franklin, IN 46131

Enterprise Fund Accounting

The Hospital uses enterprise fund accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus. Based on Governmental Accounting Standards Board (GASB) Statement No. 20, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting, as amended, the Hospital has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the consolidated financial statements. Estimates also affect the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

For the purposes of the consolidated statement of cash flows, cash and cash equivalents include demand deposits and investments in highly liquid debt instruments with an original maturity date of three months or less.

Investments

Nonparticipating certificates of deposit, demand deposits and similar negotiable instruments that are not reported as cash and cash equivalents are reported as investments at contract value which approximates fair value.

Debt securities are reported at fair value. Debt securities are defined as securities backed by the full faith and credit of the United States Treasury or fully insured or guaranteed by the United States or any United States government agency.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Mutual funds are reported at fair value based on the fund's market price. Money market investments that mature within one year or less at the date of their acquisition are reported at fair value. Other money market investments are reported at fair value. Other investments are generally reported at fair value.

Investment income (loss), including changes in the fair value of investments, is reported as non-operating revenue in the consolidated statements of revenues, expenses and changes in net assets.

Patient Accounts Receivable and Patient Service Revenues

Patient revenues and the related accounts receivable are recorded at the time services to patients are performed. Accounts receivable for patients, insurance companies, and governmental agencies are based on gross charges net of an allowance for contractual adjustments and interim payment advances. The allowance for contractual adjustments and interim payment advances is based on expected payment rates from payors based on current reimbursement methodologies. This amount also includes amounts received as interim payments against unpaid claims by certain payors. Management estimates an allowance for doubtful accounts receivable based on an evaluation of historical losses, current economic conditions, and other factors unique to the Hospital's customer base.

The Hospital is a provider of services to patients entitled to coverage under Titles XVIII and XIX of the Health Insurance Act (Medicare and Medicaid). The Hospital is reimbursed for Medicare and Medicaid inpatient services based on a fixed price per discharge for each diagnosis related grouping (DRG). The Hospital is reimbursed for Medicare and Medicaid outpatient services based on a fixed price per clinical unit of service. Differences between the total program billed charges and the payments received are reflected as deductions from revenue. At the Hospital's year-end, a cost report is filed with the Medicare program computing reimbursement amounts related to Medicare patients. The difference between computed reimbursement and interim reimbursement is reflected as a receivable from or payable to the third-party program. These programs have audited the year-end cost report filed with the Medicare program through December 31, 2006, with differences reflected as deductions from revenue in 2011. Amounts from unresolved cost reports for 2007 through 2011 are reflected in estimated third-party settlements on the consolidated balance sheets.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The Hospital did not recognize a change in net assets in 2011 and 2010 related to the differences between original estimates and subsequent revisions for the final settlement of cost reports. Laws and regulations governing the Medicare and Medicaid programs are extremely complex and subject to interpretation. Although these audits may result in some changes in these amounts, they are not expected to have a material effect on the accompanying consolidated financial statements.

Inventory

Inventory is valued at the lower of cost or market with cost being determined on the first-in, first-out (FIFO) method.

Inventory at year-end consists of the following:

	2011	2010
Medical supplies and other	\$ 1,364,829	\$ 1,350,885
Pharmaceutical	365,661	326,529
	<u>\$ 1,730,490</u>	<u>\$ 1,677,414</u>

Investments and Assets Whose Use is Limited

Investments consist of certificates of deposit and are stated at contract value. Assets whose use is limited are stated at fair market value in the consolidated financial statements. These assets include investments designated by the Hospital Board for internal purposes, investments restricted by donors for a specific purpose and investments held by trustees for debt service. These investments consist primarily of cash and cash equivalents, certificates of deposit (stated at contract value), US government securities, mutual funds and corporate stock. Investment interest, dividends, gains and losses, both realized and unrealized are included in non-operating revenue (expense) in the consolidated statements of revenues, expenses and changes in net assets.

Capital Assets and Depreciation

Capital assets such as property and equipment are stated at cost and include expenditures for new additions and other costs added to existing facilities which exceed the Hospital's capitalization policy and meet certain useful life thresholds. Maintenance, repairs and minor renewals are expensed as incurred. The Hospital provides for depreciation of property and equipment using annual rates, which are sufficient to depreciate the cost of depreciable assets over their estimated useful lives using the straight-line method.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The range of useful lives in computing depreciation is as follows:

<u>Description</u>	<u>Range of Useful Lives</u>
Land improvements	15 years
Buildings and improvements	4-50 years
Equipment	5-15 years

Net Assets

Net assets of the Hospital are classified in three components. Net assets invested in capital assets net of related debt consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. Designated net assets are net assets that are designated for a particular purpose and net assets held by the Foundation. Unrestricted net assets are the remaining net assets that do not meet the definition of net assets invested in capital assets net of related debt or designated net assets.

Consolidated Statements of Revenues, Expenses and Changes in Net Assets

The Hospital's consolidated statement of revenues, expenses and changes in net assets distinguishes between operating and non-operating revenues and expenses. For purposes of display, transactions deemed by management to be ongoing, major or central to the provision of healthcare services are reported as revenues and expenses. Non-major transactions such as investment and rental activities are reported as non-operating.

Charity Care

The Hospital provides care to patients who meet certain criteria under its charity care policy without charge or at amounts less than its established rates. Because the Hospital does not collect amounts deemed to be charity care, they are not reported as revenue. Amounts recognized as charity care as of December 31, 2011 and 2010 are approximately \$6,593,000 and \$6,433,000, respectively.

Of the Hospital's total expenses reported (approximately \$75,437,000, including interest expense, in 2011 and \$76,377,000, including interest expense, in 2010), an estimated \$2,802,000 and \$2,909,000 arose from providing services to charity patients during 2011 and 2010, respectively. The estimated costs of providing charity services are based on a calculation which applies a ratio of costs to charges to the gross uncompensated charges associated with providing care to charity patients. The ratio of cost to charges is calculated based on the Hospital's total expenses (less bad debt expense) divided by gross patient service revenue.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Federal or State Income Taxes

The Hospital is a governmental instrumentality organized under Title 16, Article 12, of the Indiana statutes. The Hospital is generally exempt from federal income tax under Section 115 of the Internal Revenue Code of 1986 as a not-for-profit organization under Section 501(c)(3). As a governmental entity, the Hospital is not required to file Federal Form 990 – Return of Organization Exempt from Income Tax which is an informational return only.

The Foundation is organized as a not-for-profit corporation under Section 501(c)(3) of the United States Internal Revenue Code. As such, the Foundation is generally exempt from income taxes. However, the Foundation is required to file Federal Form 990 – Return of Organization Exempt from Income Tax which is an informational return only. The Foundation has filed its federal and state income tax returns for periods through December 31, 2010. These income tax returns are generally open to examination by the relevant taxing authorities for a period of three years from the later of the date the return was filed or its due date (including approved extensions).

Accounting principles generally accepted in the United States of America require management to evaluate tax positions taken by the Hospital and Foundation and recognize a tax liability if these organizations have taken an uncertain position that more likely than not would not be sustained upon examination by various federal and state taxing authorities. Management has analyzed the tax positions taken by these organizations, and has concluded that as of December 31, 2011 and 2010, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the accompanying financial statements. The Foundation is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress.

Investments in Affiliates

The Hospital owns an equity interest in Johnson County Health Network, Inc., a Physician Hospital Organization. This investment is recorded on the equity method of accounting in the Hospital's consolidated financial statements. The Hospital also owned an equity interest in JMH Surgical Management Company, which operated and managed the surgery department. The Hospital dissolved JMH Surgical Management Company and received a final distribution of approximately \$149,000 during 2011.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Compensated Absences

Hospital exempt employees earn Paid Time Off (PTO) at the rate of twenty-one days to thirty-two days per year based upon the number of years of service. Hospital non-exempt employees earn PTO at the rate of fourteen days to thirty days per year based upon the number of years of service. PTO is awarded and becomes earned on the first day of the pay period following the first six months of employment and then annually thereafter on the first day of the pay period following the employee's anniversary date for PTO accrual. The maximum PTO balance allowed at any given time will be 420 hours. At termination, employees shall be awarded 50% of earned PTO up to a maximum of 150 hours.

Reclassifications

Certain amounts from the 2010 financial statements have been reclassified to conform to the current year presentation including restricted net assets of approximately \$26,367,000 from December 31, 2010 which were reclassified to designated net assets. The reclassifications have no effect on previously reported net assets or change in net assets.

Litigation

The Hospital is involved in litigation arising in the normal course of business. After consultation with the Hospital's legal counsel, management estimates that these matters will be resolved without material adverse effect on the Hospital's future financial position, results from operations or cash flows.

Risk Management

The Hospital is exposed to various risks of loss from torts; theft of, damage to, and destruction of assets; business interruption; errors and omissions; employee injuries and illnesses and natural disasters. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial coverage in any of the three preceding years.

Medical Malpractice

Malpractice insurance coverage is provided under a claims-made policy. Should the claims-made policy be terminated, the Hospital has the option to purchase insurance for claims having occurred during its term but reported subsequently. Prior to July 1, 1999, the Indiana Medical Malpractice Act provided for a maximum recovery of \$750,000 per occurrence (\$3,000,000 annual aggregate) for professional liability, \$100,000 of which would be paid through the Hospital's malpractice insurance coverage and the balance would be paid by the State of Indiana Patient Compensation Fund.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

For claims on or after July 1, 1999, the Indiana Medical Malpractice Act provides for a maximum recovery of \$1,250,000 per occurrence (\$7,500,000 annual aggregate) with the first \$250,000 covered by the Hospital's insurance and the remainder by the Fund.

Electronic Health Records (EHR) Incentive Payments

The Hospital receives EHR incentive payments under the Medicare and Medicaid programs. To qualify for the EHR incentive payments, the Hospital must meet "meaningful use" criteria that become more stringent over time. The Hospital periodically submits and attests to its use of certified EHR technology, satisfaction of meaningful use objectives, and various patient data. These submissions generally include performance measures for each annual EHR reporting period (Federal fiscal year ending September 30th). The related EHR incentive payments are paid out over a four year transition schedule and are based upon data that is captured in the Hospital's cost reports. The payment calculation is based upon an initial amount as adjusted for discharges, Medicare and Medicaid utilization using inpatient days multiplied by a factor of total charges excluding charity care to total charges, and a transitional factor that ranges from 100% in first payment year and thereby decreasing by 25% each payment year until it is completely phased out in the fifth year.

The Hospital recognizes EHR incentive payments as grant income when there is reasonable assurance that the Hospital will comply with the conditions of the meaningful use objectives and any other specific grant requirements. In addition, the financial statement effects of the grants must be both recognizable and measurable. During 2011 and 2010, the Hospital recognized approximately \$422,000 and \$-0-, respectively, in EHR incentive payments as grant income using the ratable recognition method. Under the ratable recognition method, the Hospital recognizes income ratably over the entire EHR reporting period when it is reasonably assured at the outset of the EHR reporting period that it will comply with the minimum requirements of the program.

EHR incentive income is included in other revenue in the consolidated statement of revenues, expenses and changes in net assets. EHR incentive income recognized is based on management's estimate and amounts are subject to change, with such changes impacting operations in the period the changes occur.

Receipt of these funds is subject to the fulfillment of certain obligations by the Hospital as prescribed by the programs, subject to future audits and may be subject to repayment upon a determination of noncompliance.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Subsequent Events

The Hospital evaluates events or transactions occurring subsequent to the consolidated balance sheet date for recognition and disclosure in the accompanying financial statements through the date the financial statements are issued which is March 27, 2012.

2. WINDROSE HEALTH NETWORK, INC.

The Hospital has a note receivable due from WindRose Health Network, Inc. The note is noninterest bearing, unsecured and due in monthly installments of \$8,000 through 2011. The outstanding amount due on the note as of December 31, 2011 and 2010 was \$49,490 and \$80,556, respectively.

3. NET PATIENT SERVICE REVENUE

The Hospital has agreements with third-party payors that provide for reimbursement to the Hospital at amounts different from its established rates. Estimated contractual adjustments under third-party reimbursement programs represent the difference between the Hospital's billings at standard rates and amounts reimbursed by third-party payors. They also include any differences between estimated third-party reimbursement settlements for prior years and subsequent final settlements. A summary of the reimbursement arrangements with major third-party payors is as follows:

Medicare

Medicare inpatient services are reimbursed based on a predetermined amount for each case based on the diagnosis associated with the patient (Prospective Payment Hospital). These rates vary according to a patient classification system that is based on clinical, diagnostic and other factors. The prospectively determined rates are not subject to retroactive adjustment.

The Hospital's classification of patients under the Prospective Payment Hospital and the appropriateness of patient admissions are subject to validation reviews by the Medicare peer review organization, which is under contract with the Hospital to perform such reviews. Medicare outpatient services are primarily reimbursed on predetermined rates based on the services provided.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Medicaid

The Hospital is reimbursed for Medicaid inpatient services under a prospectively determined rate-per-discharge and is not subject to retroactive adjustment. The differences between standard charges and reimbursement from these programs are recorded as contractual adjustments. Reimbursement for Medicaid outpatient services is based on predetermined rates, and is not subject to retroactive cost based settlements.

The Hospital is eligible for the Indiana Medicaid Supplemental programs including Medicaid Disproportionate Share Hospital and Municipal Upper Payment Limit programs. The Hospital recognized reimbursement from these programs within net patient revenue of approximately \$1,777,500 and \$1,850,000 in 2011 and 2010, respectively. These programs are administered by the State of Indiana, but rely on Federal funding.

Other Payors

The Hospital also has entered into payment agreements with certain commercial insurance carriers and preferred provider organizations. The basis for payment to the Hospital under these agreements includes prospectively determined rates per discharge, discounts from established charges and prospectively determined daily rates.

The following is a summary of net patient service revenue for 2011 and 2010:

	<u>2011</u>	<u>2010</u>
Patient service revenue		
Inpatient	\$ 54,538,437	\$ 52,903,164
Outpatient	<u>122,835,317</u>	<u>115,955,557</u>
Gross patient service revenue	177,373,754	168,858,721
Deductions from revenue		
Contractual allowances	98,195,013	89,442,520
Charity care	6,592,511	6,432,935
Bad debts	<u>5,375,360</u>	<u>5,550,245</u>
Total deductions from revenue	<u>110,162,884</u>	<u>101,425,700</u>
Net patient service revenue	<u>\$ 67,210,870</u>	<u>\$ 67,433,021</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

4. ASSETS WHOSE USE IS LIMITED

The classification "Assets whose use is limited" includes internally designated and Held by Foundation. Internally designated is comprised of:

- Funded Depreciation – Amounts transferred by the Hospital Board of Trustees through funding depreciation expense. Such amounts are to be used for equipment and building, remodeling, repairing, replacing or making additions to the Hospital buildings as authorized by IC 16-22-3-13.
- Capital Improvements – Amounts designated by the Board of Trustees for capital purchases and improvements.
- Other Board Designated – Amounts designated by the Board of Trustees for other specific purposes.

Assets whose use is limited that are required for obligations classified as current liabilities are reported in current assets. The composition of assets whose use is limited includes the following as of December 31:

	2011	2010
Internally designated		
Funded depreciation		
Cash and cash equivalents	\$ 16,113,015	\$ 9,867,997
Investments	2,097,378	3,867,141
Total funded depreciation	18,210,393	13,735,138
Capital improvement		
Cash and cash equivalents	642,470	2,966
Investments	1,226,039	5,741,918
Accrued interest receivable	-0-	39,669
Total capital improvements	1,868,509	5,784,553
Board designated		
Cash and cash equivalents	757,189	509,613
Investments	693,574	4,803,288
Accrued interest receivable	-0-	5
Total board designated funds	1,450,763	5,312,906
Total internally designated	21,529,665	24,832,597
Held by Foundation		
Cash and cash equivalents	59,298	138,385
Investments and other	1,483,142	1,396,470
Total held by Foundation	1,542,440	1,534,855
Total assets limited as to use	\$ 23,072,105	\$ 26,367,452

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

5. DEPOSITS AND INVESTMENTS

Deposits with financial institutions in the State of Indiana at year-end were entirely insured by the Federal Depositary Insurance Corporation or by the Indiana Deposit Insurance Fund. This includes any deposit accounts issued or offered by a qualifying financial institution.

Investments are carried at fair market value. Net realized gains and losses on security transactions are determined on the specific identification cost basis. Funded depreciation investments consist of cash equivalents and US Government securities. Market value approximated cost as of December 31, 2011 and 2010.

The Hospital's investments generally are reported at fair value, as discussed in Note 1. As of December 31, 2011 and 2010, the Hospital had the following investments and maturities, all of which were held in the Hospital's name by custodial banks that are agents of the Hospital:

December 31, 2011					
Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
US Government Securities	\$ 693,573	\$ 693,573	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit and cash	18,670,032	18,670,032	-0-	-0-	-0-
Mutual funds - equities	3,323,416	3,323,416	-0-	-0-	-0-
Foundation - cash	59,298	59,298	-0-	-0-	-0-
Foundation - fixed income obligations	170,870	-0-	115,801	42,943	12,126
Foundation - corporate stock	1,154,916	1,154,916	-0-	-0-	-0-
	<u>\$ 24,072,105</u>	<u>\$ 23,901,235</u>	<u>\$ 115,801</u>	<u>\$ 42,943</u>	<u>\$ 12,126</u>
December 31, 2010					
Carrying Amount	Investment Maturities (in years)				
	Less than 1	1-5	6-10	More than 10	
US Government Securities	\$ 4,792,455	\$ 4,087,743	\$ 704,712	\$ -0-	\$ -0-
Certificates of deposit and cash	16,038,586	16,038,586	-0-	-0-	-0-
Mutual funds - equities	4,001,556	4,001,556	-0-	-0-	-0-
Foundation - cash	138,385	138,385	-0-	-0-	-0-
Foundation - fixed income obligations	63,039	-0-	15,331	47,708	-0-
Foundation - corporate stock	1,333,431	1,333,431	-0-	-0-	-0-
	<u>\$ 26,367,452</u>	<u>\$ 25,599,701</u>	<u>\$ 720,043</u>	<u>\$ 47,708</u>	<u>\$ -0-</u>

Interest rate risk - The Hospital does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from changing interest rates.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Credit risk - Statutes authorize the Hospital to invest in interest bearing deposit accounts, passbook savings accounts, certificates of deposit, money market accounts, mutual funds, pooled fund investments, securities backed by the full faith and credit of the United States Treasury and repurchase agreements. The statutes require that repurchase agreements be fully collateralized by US Government or US Government Agency obligations.

Concentration of credit risk - The Hospital places no limit on the amount it may invest in any one issuer. The Hospital maintains its investments, which at times may exceed federally insured limits. The Hospital has not experienced any losses in such accounts. The Hospital believes that it is not exposed to any significant credit risk on investments.

Deposits and investments consist of the following as of December 31, 2011 and 2010:

	2011	2010
Carrying amount		
Deposits	\$ 12,144,615	\$ 10,326,119
Investments	24,072,105	26,367,452
	<u>\$ 36,216,720</u>	<u>\$ 36,693,571</u>
Included in the balance sheet captions		
Cash and cash equivalents	\$ 12,144,615	\$ 10,326,119
Investments	1,000,000	-0-
Internally designated	21,529,665	24,832,597
Held by Foundation	1,542,440	1,534,855
	<u>\$ 36,216,720</u>	<u>\$ 36,693,571</u>

6. FAIR VALUE MEASUREMENTS

During 2011, the Hospital changed its accounting policies to expand the level of detail provided on assets and liabilities by disaggregating mutual funds by investment objective and US Government securities, corporate bonds and corporate stocks by industry sector. The change was made to adopt Financial Accounting Standards Board's Accounting Standards Update No. 2010-06, Fair Value Measurements and Disclosures (Topic 820) - Improving Disclosures about Fair Value Measurements. Accordingly, the accounting change has been retrospectively applied to prior periods presented as if the policy had always been used.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The Hospital's investments are reported at fair value in the accompanying consolidated balance sheets. Fair value is defined as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction value hierarchy, which requires an entity to maximize the use of observable inputs when measuring fair value.

The following provides a description of the three levels of inputs that may be used to measure fair value under the standard, the types of the Hospital's investments that fall under each category and the valuation methodologies used to measure these investments at fair value.

Level 1 Fair Value Measurements

Inputs to the valuation methodology are quoted prices available in the active markets for identical investments as of the reporting date.

The fair value of mutual funds is based on quoted net asset values of the shares held by the Hospital at year-end. The net asset value is based on the value of the underlying assets owned by the fund, minus its liabilities and then divided by the number of shares outstanding. The net asset value is quoted in an active market.

The fair value of corporate stock is valued at the closing price reported on the active market on which the individual securities are traded.

Level 2 Fair Value Measurements

Inputs to the valuation methodology are other than quoted prices in active markets, which are either directly or indirectly observable as of the reporting date and fair value can be determined through the use of models or other valuation methodologies.

The fair value of US Government securities and corporate bonds is based on estimates of similar investments and the use of third party services.

Level 3 Fair Value Measurements

Inputs to the valuation methodology are unobservable inputs in situations where there is little or no market activity for the asset or liability and the reporting entity makes estimates and assumptions related to the pricing of the asset or liability including assumptions regarding risk.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The preceding methods used to measure fair value may produce an amount that may not be indicative of net realizable value or reflective of future fair values. Furthermore, although the Hospital believes its valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

Assets and liabilities measured at fair value on a recurring basis as December 31, 2011 are as follows:

	December 31, 2011			
	Total	Level 1	Level 2	Level 3
Assets				
Investments	\$ -0-	\$ -0-	\$ -0-	\$ -0-
Certificates of deposit *	1,000,000			
Total investments	<u>\$ 1,000,000</u>			
Assets whose use is limited				
Internally designated				
US Government securities				
Federal Home Loan Bank	\$ 436,245	\$ -0-	\$ 436,245	\$ -0-
Fannie Mae	257,328	-0-	257,328	-0-
Total US Government securities	<u>693,573</u>	<u>-0-</u>	<u>693,573</u>	<u>-0-</u>
Mutual funds				
Large cap value	1,006,749	1,006,749	-0-	-0-
Large cap blend	795,453	795,453	-0-	-0-
Large cap growth	700,659	700,659	-0-	-0-
Other	820,555	820,555	-0-	-0-
Total mutual funds	<u>3,323,416</u>	<u>3,323,416</u>	<u>-0-</u>	<u>-0-</u>
	4,016,989	<u>\$ 3,323,416</u>	<u>\$ 693,573</u>	<u>\$ -0-</u>
Cash equivalents and certificates of deposit *	<u>17,512,676</u>			
	<u>\$ 21,529,665</u>			
Held by Foundation				
Corporate bonds				
A rated	\$ 12,126	\$ -0-	\$ 12,126	\$ -0-
BBB rated	81,831	-0-	81,831	-0-
BB rated	51,788	-0-	51,788	-0-
B rated	25,125	-0-	25,125	-0-
Total corporate bonds	<u>170,870</u>	<u>-0-</u>	<u>170,870</u>	<u>-0-</u>
Corporate stock				
Consumer	306,575	306,575	-0-	-0-
Technology	153,649	153,649	-0-	-0-
Industrial	183,982	183,982	-0-	-0-
Other	484,995	484,995	-0-	-0-
Total corporate stock	<u>1,129,201</u>	<u>1,129,201</u>	<u>-0-</u>	<u>-0-</u>
Mutual funds - large cap growth	<u>25,715</u>	<u>25,715</u>	<u>-0-</u>	<u>-0-</u>
	1,325,786	<u>\$ 1,154,916</u>	<u>\$ 170,870</u>	<u>\$ -0-</u>
Cash equivalents and certificates of deposit *	<u>216,654</u>			
	<u>\$ 1,542,440</u>			

*Certificates of deposit are reported at contract value

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Assets and liabilities measured at fair value on a recurring basis as December 31, 2010 are as follows:

	December 31, 2010			
	Total	Level 1	Level 2	Level 3
Assets				
Assets whose use is limited				
Internally designated				
US Government securities				
Federal Home Loan Bank	\$ 3,014,362	\$ -0-	\$ 3,014,362	\$ -0-
Fannie Mae	1,778,093	-0-	1,778,093	-0-
Total US Government securities	4,792,455	-0-	4,792,455	-0-
Mutual funds				
Large cap value	1,212,175	1,212,175	-0-	-0-
Large cap blend	957,764	957,764	-0-	-0-
Large cap growth	843,628	843,628	-0-	-0-
Other	987,989	987,989	-0-	-0-
Total mutual funds	4,001,556	4,001,556	-0-	-0-
	8,794,011	\$ 4,001,556	\$ 4,792,455	\$ -0-
Cash equivalents and certificates of deposit *	16,038,586			
	<u>\$ 24,832,597</u>			
Held by Foundation				
Corporate bonds				
A rated	\$ 4,474	\$ -0-	\$ 4,474	\$ -0-
BBB rated	30,190	-0-	30,190	-0-
BB rated	19,106	-0-	19,106	-0-
B rated	9,269	-0-	9,269	-0-
Total corporate bonds	63,039	-0-	63,039	-0-
Corporate stock				
Consumer	362,024	362,024	-0-	-0-
Technology	181,438	181,438	-0-	-0-
Industrial	217,257	217,257	-0-	-0-
Other	572,712	572,712	-0-	-0-
Total corporate stock	1,333,431	1,333,431	-0-	-0-
	1,396,470	\$ 1,333,431	\$ 63,039	\$ -0-
Cash equivalents and certificates of deposit *	138,385			
	<u>\$ 1,534,855</u>			

*Certificates of deposit are reported at contract value

The following methods and assumptions were used by the Hospital in estimating the fair value of its financial instruments:

Cash and cash equivalents, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements: The carrying amount reported in the consolidated balance sheets for cash and cash equivalents, accounts payable, other current liabilities, salaries, wages and related liabilities and estimated third-party settlements approximate fair value based on short-term maturity.

Long-term debt: The fair value of the Hospital's fixed rate debt (including capital lease obligations) is estimated using discounted cash flows based on current fixed rates available to similar entities with similar credit ratings. As of December 31, 2011, the carrying value of the fixed rate long-term debt approximated its fair value.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

7. DESIGNATED NET ASSETS

Designated net assets are categorized as follows as of December 31, 2011 and 2010:

	2011	2010
Expendable - funded depreciation	\$ 18,210,393	\$ 13,735,138
Expendable - capital improvements	1,868,509	5,784,553
Expendable - other board designated	1,450,763	5,312,906
Primary government	21,529,665	24,832,597
Held by Foundation	1,540,755	1,534,855
Total designated funds	<u>\$ 23,070,420</u>	<u>\$ 26,367,452</u>

8. CAPITAL ASSETS

Capital Assets

A summary of capital assets, including assets under capital leases, as of December 31, 2011 and 2010, follows:

	December 31, 2010	Additions	Retirements	Transfers	December 31, 2011
Land	\$ 3,141,963	\$ -0-	\$ -0-	\$ -0-	\$ 3,141,963
Land improvements	1,462,057	42,040	(16,000)	-0-	1,488,097
Buildings and improvements	56,478,881	107,276	(1,623,195)	347,748	55,310,710
Equipment	40,370,215	1,637,554	(1,179,030)	959,459	41,788,198
Construction in progress	1,749,810	6,431,358	-0-	(1,307,207)	6,873,961
Total capital assets	<u>103,202,926</u>	<u>8,218,228</u>	<u>(2,818,225)</u>	<u>-0-</u>	<u>108,602,929</u>
Less accumulated depreciation:					
Land improvements	(778,885)	(76,418)	-0-	-0-	(855,303)
Buildings and improvements	(30,922,912)	(1,953,635)	1,621,553	-0-	(31,254,994)
Equipment	(31,792,279)	(2,553,804)	1,171,961	-0-	(33,174,122)
Total accumulated depreciation	<u>(63,494,076)</u>	<u>(4,583,857)</u>	<u>2,793,514</u>	<u>-0-</u>	<u>(65,284,419)</u>
Capital assets, net	<u>\$ 39,708,850</u>	<u>\$ 3,634,371</u>	<u>\$ (24,711)</u>	<u>\$ -0-</u>	<u>\$ 43,318,510</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

	December 31, 2009	Additions	Retirements	Transfers	December 31, 2010
Land	\$ 3,141,963	\$ -0-	\$ -0-	\$ -0-	\$ 3,141,963
Land improvements	1,390,763	94,216	(300,467)	277,545	1,462,057
Buildings and improvements	56,249,017	19,182	(1,112,106)	1,322,788	56,478,881
Equipment	38,237,686	945,092	(364,966)	1,552,403	40,370,215
Construction in progress	1,680,579	3,221,967	-0-	(3,152,736)	1,749,810
Total capital assets	<u>100,700,008</u>	<u>4,280,457</u>	<u>(1,777,539)</u>	<u>-0-</u>	<u>103,202,926</u>
Less accumulated depreciation:					
Land improvements	(1,013,871)	(62,581)	297,567	-0-	(778,885)
Buildings and improvements	(30,149,273)	(1,885,745)	1,112,106	-0-	(30,922,912)
Equipment	(29,457,625)	(2,644,837)	310,183	-0-	(31,792,279)
Total accumulated depreciation	<u>(60,620,769)</u>	<u>(4,593,163)</u>	<u>1,719,856</u>	<u>-0-</u>	<u>(63,494,076)</u>
Capital assets, net	<u>\$ 40,079,239</u>	<u>\$ (312,706)</u>	<u>\$ (57,683)</u>	<u>\$ -0-</u>	<u>\$ 39,708,850</u>

Depreciation expense for 2011 and 2010 amounted to \$4,583,857 and \$4,593,163, respectively. Of this amount, depreciation expense of approximately \$395,000 in 2011 and \$352,000 in 2010 is reported in rental expenses in the consolidated statements of revenues and expenses.

Construction commitments of approximately \$5,000,000 remain as of December 31, 2011.

Assets Under Capital Lease

The assets acquired through capital leases still in effect are as follows:

	2011	2010
Equipment	\$ 365,898	\$ 252,971
Less accumulated depreciation	-0-	248,628
	<u>\$ 365,898</u>	<u>\$ 4,343</u>

9. INVESTMENT IN AFFILIATED COMPANIES

The Hospital owns an equity interest in Johnson County Health Network, Inc., a Physician Hospital Organization. Additionally, the Hospital owned an equity interest in JMH Surgical Management Company, which operated and managed the surgery department. The Hospital dissolved its interest during 2011 receiving approximately \$149,000.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Summarized financial information as of December 31, 2011 and 2010 and the years then ended from the unaudited financial statements of Johnson County Health Network and JMH Surgical Management Company follows:

	Johnson County Health Network		JMH Surgical Management Company	
	2011	2010	2011	2010
Cash and cash equivalents	\$ 53,387	\$ 43,960	\$ -0-	\$ 318,058
Due from (to) Hospital	110,146	104,346	-0-	(40,589)
Total assets	<u>\$ 163,534</u>	<u>\$ 148,306</u>	<u>\$ -0-</u>	<u>\$ 277,469</u>
Liabilities	\$ 63,324	\$ 39,381	\$ -0-	\$ 20,819
Equity	100,210	108,925	-0-	256,650
Total liabilities and equity	<u>\$ 163,534</u>	<u>\$ 148,306</u>	<u>\$ -0-</u>	<u>\$ 277,469</u>
Operating revenue	\$ 19,907	\$ 27,651	\$ -0-	\$ 140,000
Nonoperating revenue	-0-	-0-	-0-	1,450
Other expenses	(28,622)	(31,100)	-0-	(122,288)
Net income (loss)	<u>\$ (8,715)</u>	<u>\$ (3,449)</u>	<u>\$ -0-</u>	<u>\$ 19,162</u>
Dividends paid	\$ -0-	\$ -0-	\$ -0-	\$ 29,716

10. LONG TERM DEBT

A summary of long-term debt as of December 31, 2011 and 2010 is as follows:

- The \$6,000,000, 2000 Variable Rate Demand Revenue Bonds were paid in full in January 2010.
- A commercial bank loan is fixed at 4.75% and is payable in monthly principal and interest payments of \$63,225 due on May 28, 2015 and is collateralized by patient accounts receivable 90 days or less.
- The Hospital has capital lease obligations with imputed interest rates ranging from 6.5% to 9.5% payable in monthly principal and interest payments ranging from \$1,023 to \$6,224 collateralized by equipment due through 2015.

The following represents a progression for long-term debt for 2011 and 2010:

	December 31, 2010	Additional Borrowings	Payments	December 31, 2011	Current Portion
Commercial bank loan	\$ 3,012,902	\$ -0-	\$ (627,348)	\$ 2,385,554	\$ 657,925
Capital lease obligations	70,301	396,372	(100,774)	365,899	120,699
Total long term debt	<u>\$ 3,083,203</u>	<u>\$ 396,372</u>	<u>\$ (728,122)</u>	<u>\$ 2,751,453</u>	<u>\$ 778,624</u>

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

	December 31, 2009	Additional Borrowings	Payments	December 31, 2010	Current Portion
Other long term debt					
Indiana Health Facility Financing Authority (IHFFA):					
\$6,000,000 2000 Demand Bonds	\$ 700,000	\$ -0-	\$ (700,000)	\$ -0-	\$ -0-
Commercial bank loan	3,610,810	-0-	(597,908)	3,012,902	627,348
Capital lease obligations	149,577	-0-	(79,276)	70,301	70,301
Total long term debt	<u>\$ 4,460,387</u>	<u>\$ -0-</u>	<u>\$ (1,377,184)</u>	<u>\$ 3,083,203</u>	<u>\$ 697,649</u>

Scheduled principal and interest repayments on long-term debt and payments on capital lease obligations for the years ending after December 31, 2011 are as follows:

Years Ending December 31,	Principal	Interest	Total
2012	\$ 778,624	\$ 145,880	\$ 924,504
2013	801,577	110,970	912,547
2014	792,598	74,271	866,869
2015	378,654	35,689	414,343
	<u>\$ 2,751,453</u>	<u>\$ 366,810</u>	<u>\$ 3,118,263</u>

11. PENSION PLAN

The Hospital offers a defined contribution plan to eligible employees. Eligibility rules for the defined contribution include 1,000 hours worked in a service year, completion of two service years and no minimum age requirement. The plan allows employee deferral contributions with the Hospital matching 50% up to 3% of eligible compensation. Additionally, the Hospital may elect to make a discretionary contribution on behalf of eligible employees. The Hospital discretionary and matching contributions to the plan are vested at 20% after 2 vesting years of service and increasing 20% every vesting year up until reaching 100% after completing 6 vesting years. The Hospital recognized approximately \$844,000 and \$896,000 during December 31, 2011 and 2010, respectively, in pension expense into the defined contribution plan.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

12. RENTAL REVENUE AND EXPENSE

The Hospital rents office space in its medical office building. Annual rental revenue for the five years following December 31, 2011 is expected to be approximately \$600,000 per year. The following is a summary of rental revenue and expense for 2011 and 2010:

	2011	2010
Rental revenue	\$ 635,649	\$ 596,971
Rental expenses		
Depreciation	395,007	352,045
Maintenance and utilities	632,803	608,437
Other	2,788	8,401
Total rental expenses	1,030,598	968,883
Rental revenue (expense), net	\$ (394,949)	\$ (371,912)

13. CONCENTRATIONS OF CREDIT RISK

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of receivables and revenue from patients and third party payors at December 31, 2011 and 2010 was as follows:

	Receivables		Revenues	
	2011	2010	2011	2010
Medicare	28%	38%	45%	43%
Medicaid	7%	6%	10%	10%
Blue Cross	12%	11%	17%	17%
Other third party payors	17%	14%	20%	22%
Self-pay	36%	31%	8%	8%
	<u>100%</u>	<u>100%</u>	<u>100%</u>	<u>100%</u>

14. BLENDED COMPONENT UNIT

The accompanying consolidated financial statements of the primary government include the blended component unit accounts of Johnson County Health Foundation, Inc. (Foundation), a separate not-for-profit entity organized to support the operations of the Hospital.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

The following is a financial summary of the Foundation as of and for the years ended December 31, 2011 and 2010:

	2011	2010
Total assets - primarily investments	<u>\$ 1,542,440</u>	<u>\$ 1,534,855</u>
Liabilities	\$ 1,685	\$ -0-
Net assets	<u>1,540,755</u>	<u>1,534,855</u>
Total liabilities and net assets	<u>\$ 1,542,440</u>	<u>\$ 1,534,855</u>
Operating revenue	\$ 4,663	\$ 6,155
Nonoperating revenue	185,320	237,081
Other expenses	<u>(184,083)</u>	<u>(120,511)</u>
Change in net assets	5,900	122,725
Beginning net assets	<u>1,534,855</u>	<u>1,412,130</u>
Ending net assets	<u>\$ 1,540,755</u>	<u>\$ 1,534,855</u>

15. RISK MANAGEMENT

Medical Benefits to Employees and Dependents

The Hospital has chosen to establish a risk-financing fund for risks associated with medical benefits to employees. The risk-financing fund is accounted for in the General Fund, where assets are set aside for claim settlements. An excess policy through commercial insurance covers individual claims in excess of \$300,000 per year with no aggregate limit. Total insurance expense for 2011 and 2010 was approximately \$3,908,000 and \$3,919,000, respectively. Settled claims resulting from this risk did not exceed commercial insurance coverage in the past three years. Provisions are also made for unexpected and unusual claims.

Claim expenditures and liabilities of the fund are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. These losses include an estimate of claims that have been incurred but not reported. These amounts are reported in accounts payable and accrued expense under current liabilities on the consolidated balance sheets.

JOHNSON MEMORIAL HOSPITAL

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS DECEMBER 31, 2011 AND 2010

Changes in balance of claim liabilities during the past two years are as follows:

	2011	2010
Unpaid claims, beginning of year	\$ 425,624	\$ 500,000
Incurred claims and changes in estimates	3,908,170	3,919,340
Claim payments	(3,808,794)	(3,993,716)
Unpaid claims, end of year	<u>\$ 525,000</u>	<u>\$ 425,624</u>

16. OPERATING LEASES

Leases that do not meet the criteria for capitalization are classified as operating leases with related rentals charged to operating as incurred. Total lease expense for 2011 and 2010 was approximately \$2,241,000 and \$2,303,000, respectively. Expected payments for the five years succeeding December 31, 2011 are approximately \$2,300,000 annually.

17. SUBSEQUENT EVENT

Subsequent to December 31, 2011, the Hospital entered into multiple agreements with two-distinct lessor entities to lease long-term care facilities operated by related management companies. Additionally, the Hospital entered into agreements with the related management companies to manage the leased long-term care facilities. As part of the agreements, the Hospital will pay the management companies a fee to continue managing the long-term care facilities on behalf of the Hospital in accordance with the terms of the agreements. While the leases are in effect, the performance of all activities of the management companies shall be on behalf of the Hospital. Furthermore, the Hospital retains ultimate authority and legal responsibility for the operation and control of the long-term care facilities. Under these agreements, all gross patient revenues from the operation of the long-term care facilities will be the property of the Hospital and the Hospital shall be responsible for all operating expenses and working capital requirements. The lease agreements expire at various times through 2016 and contain early termination clauses of 90 days which can be initiated by either party.